COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

D.T.E 05-27

BAY STATE GAS COMPANY

REQUEST FOR INCREASE IN BASE REVENUE
AND OTHER RATE MODIFICATIONS

DIRECT TESTIMONY OF DAVID J. EFFRON

On behalf of

THE OFFICE OF THE ATTORNEY GENERAL

July 13, 2005

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I. STATEMENT OF QUALIFICATIONS

Q. Please state your name and business address.

A. My name is David J. Effron. My business address is 386 Main Street, Ridgefield, Connecticut.

Q. What is your present occupation?

A. I am a consultant specializing in utility regulation.

Q. Please summarize your professional experience.

A. My professional career includes over twenty years as a regulatory consultant, two years as a supervisor of capital investment analysis and controls at Gulf & Western Industries and two years at Touche Ross & Co. as a consultant and staff auditor. I am a Certified Public Accountant and I have served as an instructor in the business program at Western Connecticut State College.

Q. What experience do you have in the area of utility rate setting proceedings?

A. I have analyzed numerous electric, telephone, gas and water rate filings in different jurisdictions. Pursuant to those analyses I have prepared testimony, assisted attorneys in rate case preparation, and provided assistance during settlement negotiations with various utility companies.

I have testified in approximately two hundred cases before regulatory commissions in Alabama, Colorado, Connecticut, Florida, Georgia, Illinois, Indiana, Kansas, Kentucky, Maryland, Massachusetts, Missouri, Nevada, New Jersey, New

York, North Dakota, Ohio, Pennsylvania, Rhode Island, South Carolina, Texas, Vermont, and Virginia.

Q. Please describe your other work experience.

A. As a supervisor of capital investment analysis at Gulf & Western Industries, I was responsible for reports and analyses concerning capital spending programs, including project analysis, formulation of capital budgets, establishment of accounting procedures, monitoring capital spending and administration of the leasing program. At Touche Ross & Co., I was an associate consultant in management services for one year and a staff auditor for one year.

Q. Have you earned any distinctions as a Certified Public Accountant?

A. Yes. I received the Gold Charles Waldo Haskins Memorial Award for the highest scores in the May 1974 certified public accounting examination in New York State.

Q. Please describe your educational background.

A. I have a Bachelor's degree in Economics (with distinction) from Dartmouth College and a Masters of Business Administration Degree from Columbia University

II. PURPOSE OF TESTIMONY

Q. On whose behalf are you testifying?

A. I am testifying on behalf of the Office of the Attorney General, Thomas F. Reilly..

Q. What is the purpose of your testimony?

A. Bay State Gas Company ("Bay State" or "the Company") has requested a base rate revenue increase and other rate modifications, including the implementation of certain rate adjustment mechanisms, in this docket. In this testimony, I address certain aspects of the Steel Infrastructure Replacement ("SIR") base rate adjustment mechanism and the Pension/PBOP expense reconciling mechanism ("PPM"). I also address certain issues in the determination of the Company's calculation of its revenue deficiency under the base rates presently in effect.

Q. Please summarize your conclusions.

A. The conclusions are as follows:

- The Department should not approve the SIR presented by the Company.
- The Department should not approve the PPM presented by the Company.

In addition, there should be certain adjustments to the determination of the Company's revenue deficiency (or excess) under present rates. In particular, there should be adjustments related to the Company's annualization/synchronization of its revenues and expenses recovered through base rates and adjustment factors, its inclusion of the Metscan amortization in the cost of service, and its proposed update to the amortization of the deferred income tax deficiency.

III. STEEL INFRASTRUCTURE REPLACEMENT

Q. Please describe the Steel Infrastructure Replacement base rate adjustment mechanism Bay State proposes.

A. The intent of the SIR base rate adjustment mechanism is to allow the Company to recover the revenue requirement associated with the SIR program, to the extent that the costs of the program exceed the bare steel replacement costs incurred in the base period of 2000 – 2003 the Company selected, without the necessity of filing a base rate case. The Company has estimated that the expenditures associated with the SIR program will be approximately $20 million per year, compared to bare steel replacement capital expenditures of about $4 million per year in the selected 2000-2003 base period.

The elements of the SIR revenue requirement are depreciation expense, property tax expense, return on net investment, and carrying costs from the in-service date to the date that rate recovery commences. The SIR rate would be adjusted annually to reflect any increase in the revenue requirement since the previous annual SIR rate was established. The SIR rate would be implemented as a component of the Company's Annual Base Rate Adjustment Mechanism ("ABRAM").

Q. Should the Department approve the SIR base rate adjustment mechanism Bay State proposes?

A. No. The SIR program base rate adjustment mechanism is unnecessary. The PBR element of the ABRAM in effect allows the Company an implicit recovery of increases in net capital investment. The PBR price cap index, which is an allowance for annual inflation offset by productivity, is applied to the Company's base rates. The base rate revenue requirement includes a return on rate base, the largest component of which is net plant in service. However, net plant in service does not grow with inflation. In fact, to the extent that annual depreciation expense is equal to or greater than additions to plant in service, the balance of net plant will be steady or even decline over time. Application of the PBR price cap index adjustment to base rates that include a return on rate base in the revenue requirement implicitly provides an allowance for capital expenditures that cause the Company's rate base to grow. The implicit allowance may well be adequate, or more than adequate, to compensate Bay State for any growth in rate base resulting from the SIR program. In addition, if expenditures related to the SIR cause the Company's earned return to fall below the bottom of the "dead band" specified in the Earning Sharing Mechanism ("ESM") feature of the PBR, Bay State is allowed to recover at least part of any such shortfall from customers.

Q. Are there problems with the base period Bay State chose for the purpose of measuring incremental expenditures of the SIR program in the future?

A. Yes. As proposed by Bay State, the SIR base rate adjustment mechanism allows the Company to recover the revenue requirement associated with the SIR program to the extent that the costs of the program exceed the bare steel replacement costs incurred in the specified base period. As can be seen on Exhibit BSG/JES-1, Schedule 17, Page 3, the Company has chosen the four years 2000 – 2003 as the base period. In response to AG 17-13, the Company provided the bare steel replacement costs for the years 1999 through 2004. That response shows that bare steel replacement costs in both 1999 and 2004 were higher than in any of the years in the 2000 – 2003 base period chosen by the Company. For example, if the Company had chosen the four years 2001 - 2004 as the base period, average base period bare steel replacement costs would have been

$4,956,000 (Schedule DJE-1) rather than the $4,041,244 shown on Schedule JES-17, Page 3 (as corrected). Thus, the Company appears to have selectively chosen a four year base period that understates the bare steel replacement costs being incurred prior to the implementation of the SIR program. This has the effect of overstating the SIR program costs that are incremental to the costs being incurred independently of the program.

Q. Would modifying the base period to incorporate the four years 2001 – 2004 or the five years 2000 – 2004 resolve the problem of comparing future expenditures to an understated base period?

A. Not necessarily. Each of those periods occurred during the merger rate freeze approved in D.T.E. 98-31. If the rate of bare steel replacement was intentionally suppressed during the rate freeze period, then the restrained spending would have two implications for the Company's proposed SIR base rate adjustment mechanism. First, using any period during the rate freeze as the base period would understate what the normal, ongoing level of bare steel replacement would be in the absence of the SIR mechanism. Second, the prospective level of bare steel replacement would have to be higher in the future to compensate for the reduced level of replacement during the rate freeze. In this regard, the response to UWUA-1-27 shows the footage of main installed in each year from 1999 through 2002 declining from the previous year. During this period, the footage of main installed decreased from 425,706 feet in 1998 to 172,237 feet in 2002, a reduction of approximately 60%. Similarly, the response to AG-2-38 shows footage of bare steel main abandoned declining in each year from 1999 through 2002 from the previous year. The footage of bare steel main abandoned decreased from 89,695 feet in 1998 to 32,162 feet in 2002, a reduction of approximately 64%. From these data, it certainly appears that the rate of bare steel replacement was being restrained during this time frame.

Q. Are there any other problems with the SIR base rate adjustment mechanism Bay State proposes?

A. Yes. As noted above, one of the elements of the SIR annual revenue requirement is carrying costs from in-service to rate recovery. This is calculated by applying the Company's authorized rate of return to the incremental SIR capital costs from the time that replacement plant goes into service until the new rates that provide a return on the cumulative SIR investment are implemented. In effect, this is post-in-service AFUDC, except that the Company includes the carrying costs in the annual revenue requirement instead of adding it to the cost of the plant and recovering it over the life of the plant. In effect, this would give the SIR program costs preferential treatment over all other capital additions. Normally, when plant is placed in service, AFUDC ceases, and the Company does not get an explicit return on that plant until its subsequent base rate case. There is no reason why the Company should be granted an explicit return on new plant investment, absent any showing that putting the plant into service has actually caused a revenue deficiency. The inclusion of the carrying costs from in-service to rate recovery in the SIR revenue requirement allows the Company to recover a revenue deficiency that may not even exist.

Another element of the SIR revenue requirement is depreciation expense on plant additions. The plant additions replace plant that is retired. When plant is retired, depreciation stops. However, as presented, the calculation of the SIR revenue requirement does not reflect the reduction to depreciation expense related to the plant retirements. I understand that the Company has agreed that the depreciation expense in the SIR revenue requirement should be adjusted to eliminate depreciation expense on retired plant (response to DTE 1-27), but that is not presently reflected in the Company's exhibits.

Q. Please summarize your testimony on the proposed SIR base rate adjustment mechanism.

A. The Department should not approve the proposed SIR base rate adjustment mechanism. There are problems in the proposed mechanism as presented by the Company, and the Company has not demonstrated that the mechanism is necessary.

IV. PENSION/PBOP EXPENSE RECONCILING MECHANISM

Q. Please describe the Pension/PBOP expense reconciling mechanism ("PPM") Bay State proposes.

A. The PPM will allow the Company to recover changes in pensions and postretirement benefits other than pension ("PBOP") through a reconciling mechanism that will be included in the local distribution adjustment clause ("LDAC"). The PPM will consist of a pension expense factor ("PEF"), representing the test year pension/PBOP expense removed from base rates plus the recovery of the difference between the current pension/PBOP expense and a return on prepaid pension costs net of applicable deferred taxes. The PPM will be recovered by a uniform per therm charge. The PPM will also reconcile the amount recovered through actual sales to the expected recovery through forecasted sales.

Q. Has Bay State established that the proposed PPM is a necessary and appropriate mechanism to implement at this time?

A. No. As a general matter, reconciliation mechanisms are contrary to sound ratemaking practice, because the mechanisms tend to either reduce or eliminate incentives to control costs either under standard ratemaking or the price cap alternative proposed by the Company. The Company presents the PPM as a reconciling mechanism that would address the volatility of pension and PBOP costs and mitigate potential financial impairment resulting from such volatility. However, the Company has not provided any measurement of the volatility of pension and PBOP costs or any measurement of how the magnitude of changes in these expenses relate to overall revenue requirements; nor has the Company compared the magnitude or volatility of pension and PBOP costs relative to other costs for which there is no adjustment mechanism.

Q. Has the Company presented any data or analysis that establishes the potential for the volatility of the pension/PBOP expense to impair its financial integrity?

A. No. Both pension and PBOP expenses are accrued by the Company pursuant to financial accounting standards[1], which require certain actuarial and financial assumptions. While it is true that changes in those assumptions can cause pension and PBOP expenses to fluctuate, just about all other expenses included in the Company's base rate cost of service are also subject to fluctuation. The Company has not adequately explained why pension and PBOP costs should be treated differently from these other expenses that go into the base rate revenue requirement. Further, the Company has not presented any analysis showing that the fluctuations in pension and PBOP costs are of such a magnitude that they have the potential to impair its financial integrity.

Q. If the Company could demonstrate that, absent the implementation of the proposed PPM, the fluctuations in the pension and PBOP pose a significant risk, is its proposal complete?

A. No. The Company does not presently have any pension and PBOP reconciliation mechanism in place, nor were any such mechanisms in place at the time of the last base rate case. Thus, to the extent the volatility of pension and PBOP expense causes financial risks, those risks are implicitly incorporated into the cost of common equity. If a reconciliation mechanism is approved, then the financial risks are transferred to the Company's customers. If the financial risks are transferred, then the Company's common stock is less risky, and the authorized return on common equity should be reduced to incorporate the reduced level of

[1] The periodic pension cost is accrued pursuant to SFAS 87, and the periodic PBOP cost is accrued pursuant to SFAS 106.

risk. If the proposed PPM is approved, then there should also be a reduction to the Company's authorized return to recognize that reduced risk.

V. REVENUE REQUIREMENT ISSUES

A. REVENUE ANNUALIZATION

Q. Have you reviewed the Company's development of the annualized revenues produced by current rates?

A. Yes. The development of the annualized revenues produced by current rates is summarized on Schedule JAF 1-1. This schedule shows the adjustments to annualize revenues produced by current direct GAF rates, current indirect GAF rates, and current DAF rates, as well as current base rates. Included in the adjustments are a weather normalization adjustment to test year volumes and an "Adjustment to Reflect Annualization." The "Adjustment to Reflect Annualization" reduces pro forma revenues under present rates by $15.2 million. In his direct testimony, Mr. Ferro describes this adjustment as including out of period adjustments, billing day determinants, and customers switching rate schedules in the test year.[2]

Q. Do you believe that these factors could reasonably result in a $15.2 million reduction to annualized test year revenues?

A. No. While the cited factors could have an effect on annualized revenues, I do not believe that an effect of $15.2 million is plausible. In fact, in the response to AG

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[2] He states that the annualization is not limited to these items but does not specify any other components of the annualization adjustment in his direct testimony.

Information Request 17-1, the Company noted that the "Adjustment to Reflect Annualization" also eliminates unbilled gas cost revenues of $12.3 million and $2.9 million of revenues from interruptible sales service.

Q. With that further explanation, is the $15.2 million adjustment plausible?

A. The $12.3 million adjustment to eliminate unbilled gas cost revenue seems to be on the high side, but it is not impossible. In any event, as long as the adjustment to eliminate unbilled gas cost revenue is properly synchronized with gas costs, and as long the adjustments to annualize revenues produced by current direct GAF rates, current indirect GAF rates, and current DAF rates are properly synchronized with the expenses related to these revenues in the determination of adjusted operating income, these annualizing adjustments will not ultimately affect the calculation of the base rate revenue deficiency. However, based on my analysis, these revenues and expenses have not been properly synchronized.

Q. Please explain.

A. Bay State has proposed numerous adjustments to actual test year revenues and expenses. Certain adjustments affect the determination of the base rate revenue deficiency. Other adjustments are more in the nature of what I would describe as being for presentation purposes. Such adjustments might shift revenue and expense between recovery through base rates and recovery through the various adjustment factors or might annualize revenues produced by adjustment factors and synchronize the test year expenses with those revenues. However, this latter group of adjustments should not ultimately affect the determination of the base rate revenue deficiency.

On my Schedule DJE-2, Page 1, I have presented an analysis of the adjustments to revenues and expenses the Company proposes. I have begun with actual 2004 test year revenues and expenses from the Company's books. Subtracting the cost of gas and other operation and maintenance ("O&M") expense from actual test year revenue, I have calculated that the actual operating margin was $87,586,000 in 2004, the Company's test year. Bay State has proposed certain adjustments to revenues and expenses for the purpose of determining its base rate revenue deficiency. The Company has also presented certain other adjustments to annualize adjustment factors and to reclassify revenues and expenses between base rates and adjustment factors. These other adjustments should not affect the determination of the base rate revenue deficiency.

On Schedule JAF 1-1, the weather normalization adjustment reduces pro forma base rate revenues produced by present rates by $2,556,000. This adjustment does affect the determination of the base rate revenue deficiency. In addition, in the response to AG 17-1, the Company has identified net adjustments of $54,000 included in the "Adjustment to Reflect Annualization" that do affect the determination of the base rate revenue deficiency.[3] As far as I can determine, the other revenue adjustments should not affect the determination of the base rate revenue deficiency and should therefore not affect the pro forma operating margin under present rates.

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[3] As I understand the response, Bay State has acknowledged an error of $405,000 in "Adjustment to Reflect Annualization" that it will correct. This analysis does not incorporate the effect of that correction.

On Schedule JAS-6, Page 1 all of the adjustments to O&M expense except the "Bad Debt Expenses – Gas Revenue" and "CGA & LDAC Recoverable Costs" affect the calculation of the base rate revenue deficiency. Adding all these other adjustments up, the total is an increase to pro forma O&M expense of $2,159,000.

With the substantive adjustments to revenue and O&M expense, the pro forma operating margin under present rates should be $82,871,000. However, as can be seen on Schedule JES-1, the pro forma operating margin under present rates calculated by the Company is only $75,385,000. There is a discrepancy of approximately $7.5 million. In other words, some $7.5 million of actual operating margin earned by Bay State in the 2004 test year disappeared in the Company's annualization process. None of the Company's descriptions of its proposed adjustments to revenues and O&M expenses explain the disappearance of this $7.5 million.

Q. Have you conducted an alternative analysis of the Company's base rate revenue deficiency?

A. Yes. I also examined the actual results of operations in the 2004 test year and calculated the Company's base rate revenue deficiency, reflecting the actual earned return on equity in 2004, the Company's requested return on equity, and its proposed adjustments to the actual results of operations in 2004.

Q. Please explain the results of this analysis.

A. The results of this analysis are summarized on my Schedule DJE-2, Page 2. In its Return to the Department for 2004, its test year in this case, Bay State indicated that it earned a return on common equity of 10.54%. The Company is requesting a return on equity of 11.50% in this case. Bay State would require additional base rate revenue of $3,459,000 to achieve a return on equity of 11.50%, exclusive of the effect of proposed adjustments to the actual results of operations in 2004 and differences between the common equity base reported in the Return and the common equity supporting rate base in this case.

As described above, the Company's proposed adjustments to revenue and O&M expense also affect its calculated base rate revenue deficiency. The identified revenue adjustments reduce the pro forma base rate revenues under present rates by $2,610,000 ($2,556,000 + $54,000) and the identified O&M adjustments increase the pro forma O&M expenses under present rates by $2,159,000. In addition, the Company has increased depreciation expense by $4,674,000 to reflect the application of its proposed new depreciation rates to the end of test year depreciable plant balances. The Company has eliminated $100,000 of amortization of Lawrence goodwill which was reflected in the Return and has proposed an adjustment to amortization expense of $2,643,000 related to the recovery of Metscan costs. Bay State has also proposed pro forma adjustments to taxes other than income taxes of $402,000. The effect of these proposed adjustments to revenues and expense other than income taxes is to increase the operating income requirement by $7,529,000. The Company's proposed adjustment to the amortization of the deferred tax deficiency increases the operating income requirement by an additional $90,000. The total effect of these adjustments to revenue and expenses is to increase the operating income requirement by $7,619,000 and the calculated base rate revenue deficiency by $12,814,000.

Finally, there are certain capital related differences between the calculation of the ROE in the Return to the Department and the cost of service in this case. The interest component of the revenue requirement in this case is $11,318,000. This is $2,599,000 greater than the interest expense of $8,719,000 reflected in the ROE calculation in the Return. On an after-tax basis, this difference in the interest expense increases the income requirement by $1,580,000. On the other hand, the common equity base used in the ROE calculation in the Return is greater than the common equity supporting the Company's rate base in this case. The lower common equity balance in this rate case (common equity X rate base) reduces the income requirement by $2,479,000. The net effect of these capital related differences is to reduce the operating income requirement by $899,000 and the calculated base rate revenue deficiency by $1,512,000.

Q. What is the base rate revenue deficiency reflecting the actual earned return in equity in 2004, the Company's requested return on equity, and its proposed adjustments to the actual results of operations in 2004?

A. I have calculated a base revenue deficiency of $14,761,000 (Schedule DJE 2, Page 2). This is $7,477,000 less than the Company's calculated base rate revenue deficiency $22,238,000. Again, there is a discrepancy of approximately $7.5 million.

Q. What do you recommend?

A. The Company's process of annualizing and synchronizing base rate revenues and costs recovered through its adjustment factors appears to have increased its calculated base rate revenue deficiency by approximately $7.5 million Unless the Company can satisfactorily reconcile this discrepancy[4], its base rate revenue deficiency should be reduced by $7.5 million by either increasing revenues or decreasing expenses. This issue is independent of any other potential adjustments to the Company's revenue requirement, such as modifications to the requested return on equity, pro forma operation and maintenance expense, depreciation expense, income taxes, and rate base.

B. METSCAN AMORTIZATION

Q. Is the Company proposing to include the amortization of costs associated with the Metscan meter reading devices in its cost of service?

A. Yes. The Company is requesting that amortization expense of $2,643,000 related to the Metscan meter reading devices be included in pro forma test year operating expenses. This includes amortization of $3,121,000 of unrecovered plant costs as of March 2005 plus amortization of what Bay State has calculated to be the present value of remaining lease payments, $10,095,000. The Company is proposing to amortize these costs over five years, which results in an annual amortization expense of $2,643,000.

[4] As noted above, the revenue adjustments include the elimination of $2.9 million of interruptible sales revenues. This would explain part of the discrepancy <u>if</u> the Company were proposing to shift interruptible sales revenues from being a credit to base rate revenues to being a credit to the cost of gas at this time. However, as I understand the response to AG 17-2, this does not appear to be the case.

Q. Should this amortization expense be included in pro forma test year operating expenses?

A. No. The Metscan devices are not presently used to provide service to customers. In addition, the expenses associated with the Encoding and Receiving Transmitters, which have replaced the Metscan devices, are included in the Company's revenue requirement. Including the costs associated with the Metscan devices in the cost of service would, in effect, require customers to pay twice for meter reading equipment over the next five years – once for equipment that is being used to provide service and once for equipment that is not being used to provide service. Accordingly, the amortization of the Metscan costs should be eliminated from the Company's revenue requirement.

Q. Are there any other reasons why the Department should not allow the Metscan amortization in the cost of service?

A. Yes. The response to DTE 01-19 shows Metscan retirements of $18,995,000 in 1997 and $825,000 in 1998. This appears to be the equipment sold and leased back by Bay State, which gave rise to the lease payments in the years 2005 – 2009 for which the Company is now seeking recovery. The response to DTE 1-20 shows proceeds from the sale of the equipment of $23,105,000. It is not clear from these documents whether the difference between the net cost of the plant retired and the proceeds from the sale was treated as salvage or was recorded as a gain[5] by Bay State. However,

[5] The gain would be calculated as the difference between proceeds from the sale and the net depreciated book cost of the plant, not the gross plant retired.

even if the proceeds were treated as salvage, this would mean, at a minimum, that the Company had a source of non-investor funds available that was never reflected in its revenue requirement during the rate freeze following D.T.E. 98-31. There has been no recognition of this benefit in the Company's quantification of the remaining Metscan costs to be recovered.[6]

In addition, to the extent that the lessor paid more for the equipment being leased back to Bay State, the lease payments would be higher. Thus, Bay State is requesting the customers to bear the cost of these higher future lease payments, while it and its shareholders have enjoyed virtually all of the cash flow benefits of the proceeds from the sale in excess of the book cost from the time of the sale-leaseback transaction until the present. This is compounded by the fact that the leases extended over an eleven year period, well beyond the expected remaining useful life of the equipment at the time that the leases were executed, and were also "back loaded." This led to lower payments initially during the merger rate freeze, which was of little benefit to customers (because there was no explicit rate recognition), but led to significantly higher lease payments in the years subsequent to expiration of the rate freeze in 2004, the payments which the Company is now seeking to recover. In other words, from all appearances, it seems that the leases were arranged to shift costs from the early years, prior to any explicit recognition of the effect of the sale-leaseback in rates, to the later years, after the rate freeze following D.T.E 98-31. Having reaped the benefits of the lower costs in the early years for itself and its shareholders, the

[6] If the excess of the sale price over the net book value of the plant sold were treated as a gain, the benefit to the Company was even greater. In that case, there would be no reduction to the remaining net book value of the equipment to be recovered for the gain, and the Company would have the whole gain to its benefit, not just the return on the proceeds until the subsequent rate case.

Company is now seeking to saddle ratepayers with the higher costs in the later years of the lease term.

Q. What is the effect of eliminating the Metscan amortization from the Company's revenue requirement?

A. The effect is to reduce the Company's revenue requirement by $2,701,000 (Schedule DJE-3).

C. AMORTIZATION OF DEFERRED TAX DEFICIENCY

Q. Is the Company proposing to update the amortization of the deferred income tax deficiency included in pro forma test year operating expenses?

A. Yes. The Company is proposing to increase the amortization by $90,000 annually to account for two changes since its last base rate case: the increment to the deficiency resulting from the 1% increase in income tax rates in 2003 and the increment to the deficiency in 2002 that was not included in the calculation of the amortization in the last case.

Q. Should the Company's calculation of the amortization be modified?

A. Yes. The Company is proposing to amortize the incremental deficiency over 13.03 years the remaining time from the end of 2004 until the end of the amortization period of the deficiency established in D.P.U. 92-111. The Company should have begun to amortize the deficiency in 1993, when it came into existence. The Company has cited no authorization to delay the commencement of amortization until this case.

If the Company had begun amortization in 1993, the amortization would be longer by 12 years, for an amortization period of 25 years. This results in annual amortization of $47,000, rather than the Company's calculated amortization of $90,000. Therefore test year pro forma income tax expense should be reduced by $43,000 (Schedule DJE-4). This has the effect of reducing the Company's revenue requirement by $73,000.

Q. Does this conclude your direct testimony?

A. Yes.